

THE ECONOMIC FRONT

LECTURE TO THE NATIONAL STRATEGY SEMINAR FOR RESERVE OFFICERS

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I appreciate the opportunity to speak to this distinguished audience and to participate in the National Strategy Seminar for Reserve Officers.

General Armstrong has quite appropriately asked me to talk about the economic front. The Soviet challenge, as you all know, is more than economic -- it is military, subversive and political as well. My remarks will of necessity touch on all these fields. I hope thereby to gain in perspective more than is lost by departing from economic purity -- if it is not a contradiction in terms to put the word "economic" next to the word "purity."

First of all, the regimes in Moscow and Peiping are governed by the principles of international Communism. Their single purpose is the liquidation of our form of free society and the emergence of a Sovietized, communized world order. The aims of international Communism, with its headquarters in Moscow, are world-wide in scope; its objectives are unlimited. Soviet leaders firmly believe, and eloquently preach, that Communism is the system which will eventually rule the world. Each move they make is directed to this end.

It follows logically that the economic development of the USSR, which is the vanguard of world Communism, is shaped to serve the needs of international Communism, not of the Soviet people.

Year after year, the proportionate diversion of economic resources to national policy purposes in the Soviet Union is without peacetime precedent in the history of the world. I define national policy purposes to include defense, research and development, foreign aid, education and investment in industry.

To promote their objectives they have determined -- cost what it may -- to develop a formidable military establishment and a strong national economy which will provide a secure home base from which to ~~display~~ their destructive foreign activities.

One can see this basic fact by examining how total output, or gross national product, was allocated in the USSR last year, and compare this with our own division of the production pie.

(Briefing Aid 1)

You can see that:

1. Soviet GNP in total was less than half that of the US -- about 45 percent of ours.
2. However, consumption, or what the consumers received in Russia, was only about one-third of the goods and services our people enjoyed. Because of the larger Soviet population, this means that on a per capita basis, the disparity in living standards was even greater than this chart shows.
3. Total Soviet investment, in contrast, was equal to about 90 per cent of our own. Their investment in industry, measured in dollars, was equal to ours. It is this long-standing practice of plowing back every ruble possible into

capital goods investment that is responsible for the rapid growth of Soviet industry. The major reasons why total U.S. investment was higher were our far greater construction of commercial facilities (shopping centers, drive-in movies and the like), and our vast road building program.

4. Finally, Soviet outlays for the military establishment were about equal to ours, in absolute dollar terms. As a proportion of gross national product, they are devoting about twice as much to military purposes as we are.

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Why so much economic effort on the Soviet military establishment?

First of all, there is the need to maintain internal security, and to keep the European Satellites in the Communist camp; to be able to deal quickly and ruthlessly with the Hungarians, the Poles and the East Germans.

Next importantly, there is a need to develop advanced weapons systems, to strive for a military breakthrough which would resolve the present nuclear stalemate in the Soviet's favor. Should the Soviets succeed in gaining clear-cut military superiority they would have a weapon for political threat and blackmail which could prove decisive, even short of a hot war.

Further, as new types of weapons are manufactured, the Communists generate large stocks of obsolescent arms that are most useful. They can be used by the Communist leaders to advance

their cause by proxy in local wars -- Korea, Vietnam, Malaya are typical examples. Also, obsolescent arms sold at cut rate prices provided the key that opened the door to Soviet influence in many underdeveloped countries. The September 1955 arms deal with Egypt was the first of these; shipments to Syria, Yemen, Afghanistan and Indonesia followed. As the world now knows, these have been profitable investments in disorder. Possession of modern armaments also is considered a source of prestige by the leaders of the new African countries, and most recently Communist arms have gone to Guinea as a gift. They were quickly followed by a military mission. There is now a considerable number of Soviet Bloc nationals in Guinea, including the inevitable trade missions. Thus, for the first time, the familiar pattern of Communist penetration is developing in the promising area of Black Africa.

I will turn now from military expenditures, and the reasons why such outlays are so high in the Soviet Union, to the subject of economic growth.

In the short space of 30 years, the Soviet Union has grown from a relatively backward nation to become the second largest industrialized economy in the world. It is true that the headlong pace of industrialization has slowed moderately in recent years. However, its growth is still well over twice that which we achieved during the decade of the 1950's.

The new confidence of Khrushchev, the shrewd and vocal leader of the Soviet Communist party, and incidentally head of government, does not rest solely on his conviction that he, too, possesses great military strength. He is convinced that the final victory of Communism can be achieved mainly by non-military means.

Khrushchev explained Soviet planned development for the next seven years in these words, to summarize the ten hours of his opening and closing remarks at the 21st Party Congress:

"The economic might of the Soviet Union is based on the priority growth of heavy industry. This will insure the Soviets victory in peaceful economic competition with capitalist countries. Development of Soviet economic might will give Communism the decisive edge in the international balance of power; it will attract millions of new adherents to our side."

We live in an unprecedented era of change. Within little more than ten years over three-quarters of a billion people, in twenty-one nations, have become independent of colonial rule. In all these newly emergent nations, there is intense nationalism coupled with the determination to achieve a better way of life. Rightly or wrongly, these peoples believe rapid industrialization is the way to progress.

In too many nations of Asia and Africa, per capita incomes average less than \$100 a year. Life expectancies are half those of the advanced nations of the west. Illiteracy is the rule, not

the exception. To these people, determined to establish quickly a decent standard living, the Soviet story of rapid economic growth has great appeal.

The leaders of world Communism are alert to the opportunity which this great transformation affords them. In their radio broadcasts to Africa, the Middle East and Asia, and through their local front organizations, the Soviets project the image of the Soviet system as the magic blueprint for achieving rapid progress. We should not underestimate the attraction which such an image has on men of influence in underdeveloped countries who are desperately seeking to lead their people into the Twentieth Century.

Let me show you one piece of Soviet propaganda, which was being used in India last year.

(Briefing Aid 2)

This chart, prepared in the Soviet Union, compares industrial growth in the USSR and in the United States in a highly exaggerated fashion.

It begins with a year of prosperity and ends with a recession period for the United States - 1948 and the first quarter of 1958.

Using 1948 as a base of 100 percent in both countries, the chart creates the impression that by 1957, Soviet output had grown five times as fast as that in the U.S. But in 1948, of course, Soviet output was still much depressed because of the war's destruction.

If you follow the line representing the U.S., you see that as this chart is made up, the first quarter decline in 1958 wiped out US production increases in recent years.

You see Uncle Sam - pot-bellied and dark-spectacled, bending backwards to view the exalted level of Soviet production. As an added bit of Socialist realism, Uncle Sam's leg is conveniently placed to hide our best years of growth.

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The Communists believe that the underdeveloped countries represent the Achilles heel of the Western World. These countries have assumed a role similar to that of the proletariat in early Marxism. To the Kremlin leaders, the Free World underdeveloped nations offer the greatest opportunities for an extension of Communism; it is the "duty" of the USSR as the vanguard of the revolution to invest some of its resources in promoting this extension.

The tactical shift in Soviet foreign policy to aid the newly emerging bourgeois governments was unveiled to the world in 1954. The party line turned from the "armed struggle" phase of the late Stalin era to a phase of "peaceful coexistence." Since then, peaceful coexistence has become more than a tactical maneuver; indeed, it is the battle itself. What is "peaceful coexistence?" In the words of former Soviet foreign minister Shepilov, and here I quote,

"Peaceful coexistence does not mean a quiet life.

As long as different social and political systems exist, contradictions between them are inevitable. Peaceful coexistence is a struggle -- a political struggle, an economic struggle, an ideological struggle."

When the Communist economic offensive started, many Western observers belittled Soviet capabilities to provide aid to underdeveloped nations. These observers believed that internal Soviet requirements for machinery and equipment, generated by the program of forced draft industrialization, would leave no surplus for export.

The judgment overlooked the fact that the Soviet Union had become a major industrial power in the world. By 1955, its annual production of industrial goods was already running over 70 billion dollars a year. Further, industrial output was increasing at an annual rate of nearly 10 percent.

It clearly follows that the Soviets possessed the industrial muscle to step up Communist activities in the Free World by economic means; all that was needed was the political decision to do so. A diversion of less than one percent of annual output was enough to support an aid program of significant proportions.

The aid program is not a large one by United States standards. Total credit extensions by the USSR over the past four years have only amounted to 1.8 billion dollars, and the net annual drain, that is the difference between drawings and repayments, has never amounted to more than half a billion dollars.

The main point is that of all Soviet outlays for national policy purposes -- defense, domestic investment, etc. -- foreign aid imposes far and away the smallest drain on resources. It could be increased substantially if the Communist leadership saw politically profitable opportunities to do so.



By 1965, the Soviets could have a foreign aid program equal to ours with still no observable strain on its economy. It seems inescapable that the economic competition will grow. This is part of what Khrushchev meant when he told Walter Lippman, "Economically speaking, we will cause you Americans more trouble every year."

Up to this point in time, Soviet Bloc aid to all under-developed countries of the Free World has been dwarfed by Western aid. However, it is important to keep in mind that Communist economic assistance is heavily concentrated in a few key target countries.

In these countries, the Soviet program is either larger than the aid provided by the United States, or is sizeable enough to be of considerable importance. Here are some examples.

(Briefing Aid 3)

1. The bars in this chart compare U.S. aid and Bloc aid from 1954 to the first quarter of 1959 for selected countries.

2. You can see that in Egypt, Syria, Iraq, Afghanistan, Ceylon and Indonesia, the Bloc has put in far more economic aid than we have. Although not shown in the chart, the same is true for Yemen.

3. In Burma, India, and Nepal, while Bloc economic aid is less than our own, it is nevertheless substantial. This applies to Cambodia as well.

These countries have been willing to expand their economic contacts with the Soviet Bloc for a variety of reasons, but a basic explanation of the success of the Soviet aid program lies in the fact that the underdeveloped countries are capital-starved. Many leaders in these countries, in fact, have voiced their suspicions of Soviet intentions, but have defended their acceptance of Bloc assistance on the ground that the great need for additional capital requirements of the underdeveloped countries will become even greater in the future, and unless the Soviets commit serious blunders, the Bloc will continue to find numerous potential outlets for its assistance offers.

So far, however, the Bloc has made some blunders but has committed relatively few major mistakes in its aid program. Its program, in fact has been cleverly formulated so as to have a general appeal to all underdeveloped countries. Each offer of assistance seems specifically designed to offer a solution to an immediate problem facing the target country.

In certain instances where the Bloc program differs from that of the U.S., the Bloc program suffers in comparison. Nevertheless, there are interesting contrasts between the Bloc and the U.S. assistance programs.

First of all, Bloc economic aid is peddled on an integrated and a continuing basis. A line of credit is offered simultaneously

with offers of technical assistance, training, and in particular, increased trade opportunities. Now, if an underdeveloped country is having difficulty in selling its products at adequate prices in the export market, the Soviet's long-term trade offers have particular appeal. Since the size of their program is not subject to annual Congressional review, the Soviets are not inhibited from signing long-term agreements. In contrast, U.S. trade is largely outside the scope of the aid program. We would find it politically difficult, if not impossible, to provide a guaranteed market for Egyptian cotton or Burmese rice, to cite only two examples.

Secondly, whereas Soviet Bloc aid is almost entirely on a credit basis, U.S. aid has consisted primarily of grants. Increasing emphasis on the Development Loan Fund, however, will probably raise the importance of credits in the U.S. program. Generally, Bloc loans carry a two and one-half percent interest rate, with repayment in goods to begin the year after the project, such as a cement plant, has been brought into production. Further, repayment prices are subject to annual negotiations, which gives the Soviets an opportunity to be tough or lenient, depending on how things are going.

Amortization on Bloc loans averages 12 years. While Western interest rates are higher, our amortization terms on loans are frequently for 20 to 40 year periods, so that the annual loan burden is lower. Moreover, if previous Western aid had taken

the form of credits rather than grants, the ability of these countries to service further loans today would in many cases be dubious.

Third, Bloc assistance is largely for industrial development -- and is intended to appeal to the desire for immediately tangible results in industrialization. It is rarely, for agricultural commodities such as under our PL 480 program, which comprises a significant part of total U.S. aid. This means that almost all of Bloc aid remains as a visible and glamorous symbol of assistance.

Fourth, the industrial development programs of the Soviets are almost always in the public sector of the economy, not the private sector. This encourages Socialist thinking on economic development, as well as stimulating government ownership rather than encouraging free enterprise.

Finally, Bloc aid programs are free of military pacts. This gives them a particular esteem in uncommitted countries. No Free World underdeveloped country receiving Bloc military or economic aid is a member of a Bloc military alliance. In contrast, most of our own aid goes to countries with which the U.S. is allied in military agreements.

In summary, the Communist aid and trade program has been designed and packaged with the target in mind. It appeals to neutralist sentiment; it provides an attractive supplement, or

in certain cases, an alternative to U.S. aid. It has no obvious strings attached to it.

However, the strings are there.

The Soviet policy of economic penetration fits like a glove into their world-wide campaign of subversion. There are over 6,000 Rlec technicians in the Free World, helping to train military forces and to build various industrial plants, the largest of which is the Indian steel mill. These technicians do not engage in propaganda or in subversive activities. Together with the Communist built plants, these technicians do serve to establish a peaceful Soviet "presence"; to lend credence to Soviet statements of disinterested help in achieving economic progress.

Meanwhile, the Communist propaganda goes out through the front organizations, directed overtly or covertly from Moscow. One of these organizations in India is the Indo-Soviet Cultural Society. Let's take a look at it.

(Briefing Aid 4)

1. You can see that this Indo-Soviet Cultural Society virtually blankets the country.
2. Several of its branches are located in Madhya Pradesh State, where the Russian-built steel mill is being completed.
3. Communist propaganda, similar to the slide I showed you earlier, comparing U.S. and USSR industrial growth, is distributed by such front organizations.

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What you have seen on this slide is only one Communist front organization. But the Soviets and their Chinese Communist allies have organized a vast number of fronts, covering almost every branch of human enterprise. They include youth and student groups, labor and veterans organizations, women's groups, and, of course, the World Peace Council with its innumerable peace societies. In total, the claimed membership of all fronts runs into several hundred million people.

In addition to the front organizations, and native Communist parties, as devices to spread the arguments for Communism, massive radio programs are beamed daily to Africa, Asia and the Middle East. These are heard in scores of languages. They come from clandestine transmitters as well as those which are openly acknowledged.

There is no set pattern to these messages. Moscow carefully tailors broadcasts to fit the particular vulnerabilities of each target area and audience.

I stress this point because one of the objectives of the Sino-Soviet Bloc aid program is to place its radio broadcasting equipment in underdeveloped areas. Complete radio stations are offered either at cut prices under very liberal credit terms or as a gift. Bloc technicians are always employed in the survey, installation and initial operating stages of these projects.

What does Bloc hope to gain by having its transmitters installed in underdeveloped countries?

At the minimum, the Soviets expect that broadcast facilities will be used by nationalist leaders to push anti-Western revolutionary themes.

Actually the Soviets have little trouble in finding within the emerging countries cabinet members or other leaders sympathetic to Communism. Charges of brutality by Western colonial powers not only please Moscow but undoubtedly are more persuasive to local populations when broadcast from one of their own countries than when beamed from Moscow.

At the maximum, the leaders of the Bloc hope that, by installing radio stations, they will receive the right to broadcast their own program material on these stations. For example, the Chinese Communists have presented Cambodia with a gift of a radio transmitter. Now the Chinese are trying to get the Cambodians to allocate several hours a day for rebroadcasts of Peiping radio programs.

I would like to show you where the Bloc has built or is offering to build broadcasting facilities in the Free World.

(Briefing Aid 5)

1. First of all, there are the two stations in Egypt with two more to come. There are two scheduled for Syria, and the other member of the UAR. Perhaps this investment does not look as profitable to Moscow today as it did a year ago.

2. However, the USSR is now putting up four transmitters in Iraq, where the Communists are a most powerful force in and out of the government.

3. Moving from the Middle East to Africa, you can see the offer of a transmitter to Guinea. Rumors suggest that other newly emergent African nations will receive similar offers.

4. The Cambodian station, supplied by China, I have already mentioned.

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I will turn now from the Communist aid program to the subject of Bloc trade with the Free World.

In my opinion, there is a sharp and clear cut difference in motivation between Communist trade with the industrial West and Communist trade with the underdeveloped countries of the Free World.

Most Soviet trade with the Free World is with the industrial West. The Russians seek to buy chemical equipment, electronics and automation equipment, tire plants, and are interested in purchasing facilities to improve their ferrous metallurgical industry. This trade is motivated primarily by internal economic considerations, not by its political impact on the West. Soviet imports of machinery from Europe, embodying advanced technology, are important to the rapid expansion of Communist industry in certain key areas. This was frankly admitted by Khrushchev when he stated that through such imports; and here I quote,

"The Soviet Union could be given the opportunity of quicker fulfillment of its program .... without wasting time."



Increased imports from the West mean increased Soviet exports of a lengthening list of raw materials, fuels and semi-manufactured goods. These are the Soviet goods available for export that Europe will buy. There is no market for Soviet machinery in Germany, for example, or for Soviet textiles in England.

From time to time, Soviet sales of tin and aluminum at low prices have brought charges of "dumping" from Free World suppliers of these materials. However, such charges overlook the fact that Soviet sales of industrial raw materials to Europe are designed to gain foreign exchange needed to pay for increased imports of machinery. The Soviets have always charged as much as they thought the market would bear. When in 1958 Western commodity markets were experiencing a recession, Russian prices were low; the recent rise in platinum prices, however, was led by Soviet sellers. In my opinion, the Soviets have nothing to gain by disorganizing markets and driving prices down in this area -- on the contrary, lower prices mean that more Soviet materials have to be sent to secure a given amount of foreign exchange.

I stress this because a distortion of Soviet motives does no one any good in the long run. It just confuses the issue. The political challenge of International Communism in Western Europe has been met and turned back. Stimulated by Marshall Plan aid, Western Europe has undergone rapid economic growth over the past decade; unemployment has largely disappeared, most currencies are

strong and stable and Communist parties have lost strength everywhere.

Soviet trade with the underdeveloped nations is a very different matter. It is motivated primarily by its political impact on the areas concerned. Its ultimate motivation is to export Communism. For example, a year ago Khrushchev stated,

"Another form of relations is that obtaining between Socialist countries and the economically underdeveloped countries. One may not of course say that in this case that our economic relations are based on mutual advantage. Speaking generally from the commercial viewpoint, our economic and technical aid to the underdeveloped countries is even unprofitable for us."

Soviet motivation behind much of the recently created trade activity between the Communists and the newly independent countries is, ultimately, to bring these countries into what Moscow calls, "the Socialist camp." This is not to be done in one step, of course.

The initial stage consists of replacing traditional Western trade in these areas by Soviet Bloc trade. This has already been done in a limited number of countries. For example, Iceland's fish now goes to the Soviet Bloc, not to the United Kingdom. Over 60 percent of Egypt's cotton exports are now to the Bloc, not to Western Europe. Iraq is currently deriving more and more of its imports from the Bloc, less from the West. Soviet oil is now crucial to several small countries, and all nations receiving Soviet plant and equipment must return to the Bloc for maintenance and spare parts.

Once again, the Soviet's effort is highly selective. About 80 percent of total Bloc trade in underdeveloped areas is with only 16 countries. Further, the same pattern of concentration which I spoke of earlier in Bloc aid is also true of Bloc trade -- a concentration on key target countries.

These expanded trade activities are, moreover, based on highly complementary economies. What the underdeveloped countries have to sell is overwhelmingly food, fibers, and industrial raw materials, products which can easily be absorbed by the Bloc. The European Satellites as a whole are now a deficit food producing area, and always were dependent upon imports for raw materials. The present low level of per capita consumption in the Soviet Bloc implies a great capacity for absorbing the exports of many underdeveloped countries.

It follows logically that with the shift in marketing patterns, the Soviet presence in the underdeveloped areas grows while that of the West diminishes. If Bloc economic blandishments and the massive use of propaganda do not lead to an increase in the domestic appeal of Communism over time, there is no reason to believe that the Soviets will hesitate to use economic pressure to bring about a state of affairs more to their liking. Once the economic vulnerability has been created, its exploitation along with other Soviet devices, is a matter of timing.

There are many fresh examples of the use of trade as a weapon by the Soviet Union.

Within recent months, the Soviets have threatened to cut off trade with Greece if that nation allows NATO missile bases to be established on her territory.

Pressure from Moscow for a Soviet-Iranian non-aggression pact was backed up this year by the withholding of orders for Iranian lead and zinc ores, for which the traditional market has been the USSR.

Last December, the Finnish government fell, a victim of Finland's vulnerability to Soviet economic pressure. Angered by efforts of the Finnish government to move closer to the West, the Soviets were quick to react. They cut off petroleum supplies, cancelled orders for manufactured goods and refused to negotiate a trade agreement. Soviet economic pressure was skillfully coordinated with political pressure by the Finnish Communist Party and with strong attacks by Soviet press and radio on the government of Finland. From the beginning of the Moscow drive to the toppling of the Fagerholm government took only two months.

To summarize this somewhat rambling presentation on the economic front, the following points appear to me most important:

1. The Soviets, year in and year out, devote a very large percentage of their economic resources to purposes of national policy, most prominently to defense and investment in heavy industry.

2. As a result, they have achieved a rapid rate of economic development which now not only provides them with the economic muscle needed to promote the external expansion

of Communism, but also serves as a powerful propaganda weapon in selling Marxism to the peoples of the underdeveloped countries.

3. The ability to provide arms at cut rate prices and development capital on attractive repayment terms opens the door to the spread of Communist economic influence in key underdeveloped countries. In these countries a pressure to reorient trade away from the West to the Bloc inevitably follows.

4. Bloc economic penetration, to be understood, must be examined in the light of the total Soviet offensive -- including their propaganda, subversion, and political penetration -- in the underdeveloped nations. Trade and aid establish the Soviet presence and provide a plausible front of disinterested helpfulness.

5. The Soviet leaders frankly admit that their motivation in economic dealings with the new and fragile democracies is ultimately to move these countries beyond neutralism into the Communist empire. Once a condition of vulnerability has been brought about, history clearly shows the Kremlin will take advantage of its bargaining position.